

THE OFFICE OF REGULATORY STAFF

DIRECT TESTIMONY

OF

HENRY N. WEBSTER, II

DECEMBER 10, 2010



DOCKET NO. 2010-132-W

**Application of May River Water Company,
Inc. for Adjustment of Rates and Charges for
the Provision of Water Service**

DIRECT TESTIMONY OF HENRY N. WEBSTER, II

FOR

THE OFFICE OF REGULATORY STAFF

DOCKET NO: 2010-132-W

**IN RE: APPLICATION OF MAY RIVER WATER COMPANY, INC. FOR
ADJUSTMENT OF RATES AND CHARGES FOR THE PROVISION OF WATER
SERVICE**

**Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND
OCCUPATION.**

A. My name is Henry N. Webster, II. My business address is 1401 Main Street, Suite 900, Columbia, South Carolina, 29201. I am employed by the South Carolina Office of Regulatory Staff ("ORS") as an Auditor.

**Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND
EXPERIENCE.**

A. I received a Bachelor of Science degree with a major in Accounting and minor in English from Bob Jones University in 1983. I am a Certified Public Accountant licensed to practice in South Carolina, with over 24 years of professional work experience in public accounting, internal audit, various controller and financial management roles. In 2008, I began my employment with ORS, where I have been performing regulatory reviews of utility companies, focused primarily upon rate cases and new nuclear deployment.

1 **Q. ARE YOU CURRENTLY A MEMBER OF ANY PROFESSIONAL**
2 **ORGANIZATIONS?**

3 **A.** Yes. I hold memberships in good standing with the South Carolina
4 Association of Certified Public Accountants, the American Institute of Certified
5 Public Accountants, and the Institute of Management Accountants, where I have
6 served multiple terms as chapter board member and committee chairman.

7 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
8 **PROCEEDING?**

9 **A.** The purpose of my testimony is to set forth my findings and
10 recommendations resulting from ORS's examination of the application of May
11 River Water Company, Inc. ("May River", "Applicant" or "MRWC") in this
12 docket. The application was filed on September 8, 2010.

13 **Q. PLEASE IDENTIFY THE EXHIBITS ATTACHED TO YOUR**
14 **TESTIMONY.**

15 **A.** I have attached the following exhibits to my testimony relating to the
16 Application of May River Water Company, Inc.:

- 17 • Audit Exhibit HNW-1: Operating Experience and Operating Margin
18 • Audit Exhibit HNW-2: Explanation of Accounting and Pro Forma
19 Adjustments
20 • Audit Exhibit HNW-3: Depreciation Expense Adjustment
21 • Audit Exhibit HNW-4: Computation of Income Taxes

22 These exhibits were either prepared by me, or under my direction and supervision,
23 in compliance with recognized accounting and regulatory procedures for water

1 utility rate cases. These exhibits show various aspects of May River's operations
2 and financial position.

3 **Q. PLEASE DESCRIBE THE FORMAT OF AUDIT EXHIBIT HNW-1 AND**
4 **ELABORATE ON THE CALCULATIONS.**

5 **A.** Audit Exhibit HNW-1 shows May River's operating experience and
6 operating margin for water operations for the test year ended December 31, 2009.
7 The exhibit's format is designed to reflect the Application per books and ORS's
8 proposed accounting and pro forma adjustments necessary to normalize the results
9 of May River's test year operations.

10 Column (1) shows the Application per books calculated by May River for the test
11 year ended December 31, 2009.

12 Column (2) shows ORS's proposed accounting and pro forma adjustments designed
13 to normalize the Application per books. An explanation of each adjustment is
14 contained in Audit Exhibit HNW-2.

15 Column (3) shows ORS's result of a normalized test year for May River by adding
16 columns (1) and (2). After the accounting and pro forma adjustments, Net Loss for
17 Return of (\$11,598) was computed using Total Operating Revenues of \$12,465,
18 less Total Operating Expenses of \$24,063.

19 Column (4) shows the applicant's proposed increase in revenue recalculated by
20 ORS, and the calculation of taxes associated with the proposed increase. An
21 explanation of each adjustment is contained in Audit Exhibit HNW-2.

1 other wage data provided by Applicant. ORS further considered other direct costs
2 which included billing stock, postage and travel expenses incurred by WUM in
3 performance of its duties to arrive at total direct costs of \$14,329.

4 Additional analysis was performed on WUM's overhead to determine an
5 appropriate level of indirect expense to be allocated to the Company using a
6 supportable basis. The resulting pool of acceptable WUM overhead totaled
7 \$451,752, allocated on a basis of total May River customer accounts of 30 (28
8 active accounts, and 2 unmetered lots), over a WUM customer count for all systems
9 of 11,953 (9,450 active customers, 673 vacant houses, and 1,830 unmetered lots).
10 The calculation resulted in an allocation factor of .2509%, or \$1,134 of indirect
11 costs allocated to May River. ORS's total computed costs for management contract
12 services consisted of direct costs of \$14,329 and indirect costs of \$1,134, totaling
13 \$15,463. When compared to the Company's requested total of \$27,000, the
14 resulting adjustment is (\$11,537).

15 Adjustment 5 – ORS proposes to amortize rate case expenses incurred for this rate
16 case proceeding over three years. ORS verified documented rate case expenses of
17 \$4,372 as of December 3, 2010. This amount, which included legal expenses and
18 the cost for publishing the notice of filing and hearing, was amortized over the
19 three-year period, resulting in the test year expense of \$1,457. Applicant proposed
20 total rate case expenses of \$4,000, resulting in amortization expense of \$1,333.

21 Adjustment 6 – ORS proposes to reduce Miscellaneous Expense by (\$155) for two
22 registration charges required by the State of Georgia, since MRWC's parent
23 company is headquartered in Georgia. The non-regulated expenses are not

1 associated with South Carolina, and therefore, not included in Total Operating
2 Expense.

3 Adjustment 7 – ORS proposes to annualize Depreciation Expense using service
4 lives recommended by ORS’s Water and Wastewater witness Hannah K. Majewski.
5 The details of the Depreciation Expense adjustment are shown in Audit Exhibit
6 HNW-3. ORS’s total Depreciation Expense amounted to \$212, less the per book
7 amount of \$551, for a total adjustment of (\$339).

8 Adjustment 8 – ORS proposes to reduce Taxes Other Than Income associated with
9 the revenues after ORS’s accounting and pro forma adjustments. ORS used a
10 factor of .00946, which is composed of the ORS/PSC (“Public Service
11 Commission”) factor of .00646, and the Department of Revenue’s factor of .003.
12 ORS’s total adjustment is (\$10) ($\$12,465 \times .00946$, less \$128 on Applicant’s
13 books).

14 Adjustment 9 – Based upon ORS Water and Wastewater Department calculations,
15 May River’s proposed rates would produce additional Metered Sales - Residential
16 of \$26,487. Details of this adjustment are shown in direct testimony of ORS Water
17 and Wastewater witness Hannah K. Majewski.

18 Adjustment 10 – ORS proposes to adjust Unmetered Sales – Residential by \$384.
19 Details of the adjustment are shown in the direct testimony of ORS Water and
20 Wastewater witness Hannah K. Majewski.

21 Adjustment 11 – ORS proposes to adjust Taxes Other Than Income associated with
22 the revenues after the proposed increases. ORS used a factor of .00946, which is
23 composed of the ORS/PSC factor of .00646, and the Department of Revenue’s

1 factor of .003. ORS's total adjustment is \$254 (\$39,336 x .009460234, less the
2 \$118 balance after ORS's proposed adjustments).

3 Adjustment 12 – ORS proposes to adjust Income Taxes by \$2,891 associated with
4 the applicant's proposed rate increase. See Audit Exhibit HNW-4 for the
5 computation of Income Taxes.

6 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

7 A. Yes.

May River Water Company, Inc.
Docket No. 2010-132-W
Operating Experience and Operating Margin
For the Test Year Ended December 31, 2009

	(1)	(2)	(3)	(4)	(5)
	Application Per Books	ORS's Proposed Accounting & Pro Forma Adjustments	After ORS's Proposed Accounting & Pro Forma Adjustments	Applicant's Proposed Increase	After Applicant's Proposed Increase
<u>Operating Revenues</u>					
Metered Sales - Residential	\$ 11,400	\$ 681 (A)	\$ 12,081	\$ 26,487 (I)	\$ 38,568
Unmetered Sales - Residential	384	0	384	384 (J)	768
<u>Total Operating Revenues</u>	\$ 11,784	\$ 681	\$ 12,465	\$ 26,871	\$ 39,336
<u>Operating Expenses</u>					
Purchased Power	\$ 796	\$ 0	\$ 796	\$ 0	\$ 796
Materials and Supplies	10	(10) (B)	0	0	0
Contract Labor - Professional	1,074	0	1,074	0	1,074
Contract Labor - Water Testing	2,114	(25) (C)	2,089	0	2,089
Contract Labor - WUM LLC	27,000	(11,537) (D)	15,463	0	15,463
Rents	2,760	0	2,760	0	2,760
Regulatory Commission Expense	60	1,457 (E)	1,517	0	1,517
Miscellaneous Expense	189	(155) (F)	34	0	34
Depreciation Expense	551	(339) (G)	212	0	212
Taxes Other Than Income	128	(10) (H)	118	254 (K)	372
Income Taxes	0	0	0	2,891 (L)	2,891
<u>Total Operating Expenses</u>	\$ 34,682	\$ (10,619)	\$ 24,063	\$ 3,145	\$ 27,208
<u>Net Operating Income (Loss) for Return</u>	\$ (22,898)	\$ 11,300	\$ (11,598)	\$ 23,726	\$ 12,128
<u>Operating Margin</u>	<u>-194.31%</u>		<u>-93.04%</u>		<u>30.83%</u>

May River Water Company, Inc.
Docket No. 2010-132-W
Explanation of Accounting and Pro Forma Adjustments
For the Test Year Ended December 31, 2009

Revenues and Expenses	Adj.#	Description	\$ ORS	\$ Applicant
<u>Accounting and Pro Forma Adjustments</u>				
(A) Metered Sales - Residential	1	To normalize customer billings for the test year.	<u>681</u>	<u>0</u>
(B) Materials and Supplies	2	To adjust for expenses incurred outside the test year.	<u>(10)</u>	<u>0</u>
(C) Contract Labor - Water Testing	3	To adjust for expenses incurred outside the test year.	<u>(25)</u>	<u>0</u>
(D) Contract Labor - WUM LLC	4	To adjust for allowable costs incurred under the management operating agreement.	<u>(11,537)</u>	<u>0</u>
(E) Regulatory Commission Expense	5	To adjust for rate case expenses amortized over three years.	<u>1,457</u>	<u>1,333</u>
(F) Miscellaneous Expense	6	To adjust for non-regulated expenses.	<u>(155)</u>	<u>0</u>
(G) Depreciation	7	To adjust depreciation expense on fixed assets.	<u>(339)</u>	<u>0</u>
(H) Taxes Other Than Income	8	To adjust the gross receipts taxes associated with ORS's accounting and pro forma adjustments.	<u>(10)</u>	<u>0</u>
(K) Income Taxes (State and Federal)	12	To adjust income taxes associated with ORS's accounting and pro forma adjustments.	<u>-</u>	<u>0</u>
<u>Proposed Increase</u>				
(I) Metered Sales - Residential	9	To adjust customer billings for ORS's calculation of the proposed rate increase.	<u>26,487</u>	<u>26,017</u>
(J) Unmetered Sales - Residential	10	To adjust customer billings for ORS's calculation of the proposed rate increase.	<u>384</u>	<u>384</u>
(K) Taxes Other Than Income	11	To adjust gross receipts taxes associated with the proposed rate increase.	<u>254</u>	<u>0</u>
(L) Income Taxes (State and Federal)	12	To adjust income taxes associated with the proposed rate increase.	<u>2,891</u>	<u>868</u>

May River Water Company, Inc.
Docket No. 2010-132-W
Depreciation Expense Adjustment
For the Test Year Ended December 31, 2009

Date Acquired	Description	Amount	Service Life (in years)	Rate	Expense
<u>May River Plantation Improvements</u>					
<u>Note 1</u>		<u>Note 2</u>			
01/01/08	Well Site	\$ 3,051	27	3.70%	FD
01/01/08	Distribution System	3,268	38	2.63%	FD
01/01/08	Tank	3,268	20	5.00%	FD
01/01/08	Building and Electric	2,179	25	4.00%	FD
01/01/08	Pump and Motor	872	17	5.88%	FD
01/01/08	Fence	1,450	15	6.67%	97
	Totals	<u>\$ 14,088</u>			<u>\$ 97</u>
<u>Equipment</u>					
02/15/08	Transit Time Flow	1,720	15	6.67%	115
	Total Fixed Assets & Depreciation Expense	<u>\$ 15,808</u>			<u>\$ 212</u>
	Less: Per Book Depreciation Expense				(551)
	ORS's Proposed Depreciation Expense Adjustment				<u>\$ (339)</u>

Notes:

- (1) In accordance with PSC Order No. 2009-66, MRWC was separated from South Atlantic Utilities, Inc. effective 1-1-2008. Several of the May River assets that transferred were fully-depreciated, as noted above. Only the fence and the transit time flow are still being depreciated under this docket.
- (2) The service lives used in the calculations above were provided by the ORS Water and Wastewater Department.

"FD" = Fully Depreciated

May River Water Company, Inc.
Docket No. 2010-132-W
Computation of Income Taxes
For the Test Year Ended December 31, 2009

	After ORS's Proposed Accounting & Pro Forma Adjustments	After Applicant's Proposed Increase
Total Operating Revenues	\$ 12,465	\$ 39,336
Less: Operating Expenses	<u>24,063</u>	<u>24,317</u>
State Taxable Income	(11,598)	15,019
Less: State Income Taxes @ 5%	<u>0</u>	<u>751</u>
Federal Taxable Income	(11,598)	14,268
Federal Income Taxes: 1st \$50,000 @ 15%	<u>0</u>	<u>2,140</u>
ORS's Income Taxes (State and Federal) Adjustment	<u><u>\$ 0</u></u>	<u><u>\$ 2,891</u></u>